

Message Text

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ACTION EUR-25

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-07 H-03 INR-10 L-03

NSAE-00 NSC-07 PA-04 RSC-01 PRS-01 SP-03 SS-20

USIA-15 AID-20 COME-00 EB-11 FRB-02 TRSE-00 XMB-07

OPIC-12 CIEP-02 LAB-06 SIL-01 OMB-01 AGR-20 STR-08

CEA-02 SCI-06 INT-08 FEA-02 FPC-01 DRC-01 /210 W

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TO SECSTATE WASHDC 3873

C O N F I D E N T I A L OTTAWA 2055

E.O. 11652: GDS

TAGS: PINT, PFOR, CA

SUBJECT: SECOND QUARTER REPORT 1974 - CANADA.

REF : OTTAWA 0877

1. SUMMARY: FOLLOWING THE TRUDEAU GOVERNMENT'S DEFEAT ON THE BUDGET, MAY 8, FEDERAL ELECTIONS WERE CALLED FOR JULY 8, WITH THE OUTCOME STILL VERY MUCH IN DOUBT. THE PRINCIPAL ISSUE IN DEBATE IS THE CONTINUED INFLATION AND THE RISING COST OF LIVING, WHICH SHOW NO SIGN OF ABATING AND FOR WHICH NO PARTY OR POLITICAN HAS YET DEMONSTRATED TO THE ELECTORATE A PERSUASIVE ANSWER. NEVERTHELESS, AND PERHAPS IN PART A FUNCTION OF THE WEATHER, THERE IS A SENSE OF SOME OPTIMISM OR EVEN COMPLACENCY IN CANADA TODAY. THERE IS GOOD REASON FOR THIS ATTITUDE. THE CANADIAN ECONOMY IS DOING AT LEAST AS WELL AS PREDICTED IN MARCH. REAL GNP GROWTH IN THE FIRST QUARTER WAS AT AN ANNUAL RATE OF ALMOST SEVEN PERCENT. WHILE THERE IS TWO-DIGIT INFLATION, A NAGGING CONCERN WITH THE RATE OF UNEMPLOYMENT, WORRY OVER THE IMPACT OF MASSIVE WAGE SETTLEMENTS AND SPREADING LABOR UNREST, AND SOME UNCERTAINTY IN THE BUSINESS COMMUNITY

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REGARDING, FOR EXAMPLE, FUTURE TAX TREATMENT OF RESOURCE

INDUSTRIES AND THE IMPACT OF NEW SCREENING PROCEDURES ON FOREIGN INVESTMENT, CONSIDERING THE POLITICAL AND ECONOMIC PROBLEMS FACING MOST OTHER INDUSTRIAL NATIONS, CANADIANS CAN BE FORGIVEN FOR FEELING A BIT SMUG. THEIR AGRICULTURAL AND MINERAL RESOURCE BASE IS AS SOLID AS ANY IN THE WORLD, THEIR POLITICAL PROCESS RELATIVELY ORDERLY, UNEXCITING, AND FREE FROM SCANDAL, AND THEIR INTERNATIONAL IMAGE GENERALLY GOOD.
END SUMMARY

2. BILATERAL RELATIONS. SUBSTANTIAL PROGRESS HAS BEEN ACHIEVED IN SEVERAL AREAS: THE BILATERAL AIR AGREEMENT WAS SIGNED MAY 8 AFTER YEARS OF DIFFICULT NEGOTIATIONS; BILATERAL DISCUSSIONS OF RAILROAD ROLLING-STOCK EXCHANGES ARE PROCEEDING AMICABLY; THE OIL SPILL CONTINGENCY PLAN WAS SIGNED MAY 19; NOTES HAVE BEEN EXCHANGED ON WEST COAST ENVIRONMENTAL PROTECTION; AND A SUCCESSFUL STOCK-TAKING MEETING WAS HELD IN WASHINGTON ON PERFORMANCE IN IMPLEMENTING THE GREAT LAKES WATER QUALITY AGREEMENT. NEVERTHELESS, AND TYPICAL OF THE SENSITIVE AND PERVASIVE NATURE OF CANADA'S RELATIONS WITH THE US, SECRETARY BUTZ' SUGGESTION OF RETALIATION SHOULD GOC NOT AGREE TO PROCEDURES FOR CERTIFICATION THAT US BEEF TO BE EXPORTED TO CANADA IS FREE OF THE GROWTH HORMONE DES, HAS MADE HEADLINES IN THE NEWS MEDIA, RAISED HACKLES IN OFFICIAL CIRCLES, AND EXACERBATED THE PROBLEM OF REACHING AN ACCOMMODATION THAT WILL NOT BE PORTRAYED IN CANADA AS "KNUCKLING UNDER." PROVINCIAL LAND EXPROPRIATION MEASURES IN EAST, CENTRAL, AND WESTERN CANADA MAY ALSO CAUSE MORE TRANS-BORDER FRICTION.

3. DOMESTIC POLITICS. THE NEW DEMOCRATIC PARTY (NDP), WHICH HAD SUPPORTED THE LIBERAL MINORITY GOVERNMENT FOR ALMOST 18 MONTHS, WITHDREW ITS SUPPORT MAY 8 AND VOTED WITH THE PROGRESSIVE CONSERVATIVE (PC) OPPOSITION TO DEFEAT THE GOVERNMENT'S BUDGET. PARLIAMENT WAS DISSOLVED, AND ELECTIONS WILL BE HELD JULY 8. PREDICTIONS ARE EXTREMELY CHANCY, AND MOST OBSERVERS EXPECT ANOTHER MINORITY GOVERNMENT LED EITHER BY TRUDEAU OR PC LEADER STANFIELD. STANFIELD HAS MADE INFLATION THE MAJOR ISSUE, BUT HIS PROPOSALS TO COPE WITH IT -- A TEMPORARY WAGE AND PRICE FREEZE -- HAVE BEEN ILL-EXPLAINED AND UNCONVINCING.
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WHICHEVER WAY THE VOTE GOES, THERE IS LITTLE OR NO LIKELIHOOD OF MAJOR SHIFTS IN CANADIAN FOREIGN POLICIES, OR IN CANADA'S RELATIONS WITH THE US. A PC MINORITY GOVERNMENT WOULD PROBABLY BE LESS ABLE TO SECURE NDP SUPPORT THAN WOULD THE LIBERALS, AND ANOTHER ELECTION MIGHT RESULT AS EARLY AS NEXT WINTER.

4. THE ECONOMY. WHILE THE CANADIAN ECONOMY IS

ESSENTIALLY IN EXCELLENT SHAPE, THERE ARE STILL PROBLEMS AHEAD. MINFIN TURNER'S ABORTED FEDERAL BUDGET ZEROED IN ON RECENT HIGH PROFITS IN CANADIAN RESOURCES INDUSTRIES BY PROPOSING AN INCREASE IN CORPORATE TAX ON MINERALS, OIL AND GAS, REDUCING DEPLETION ALLOWANCES, AND DISALLOWING PROVINCIAL ROYALTIES, MINING TAXES AND SIMILAR PAYMENTS AS FEDERAL TAX DEDUCTIONS BY MINING AND PETROLEUM CORPORATIONS. THESE PROPOSALS, COUPLED WITH SUBSTANTIAL INCREASES IN RESOURCES TAXED AND ROYALTIES EFFECTED OR UNDER SERIOUS CONSIDERATION IN THE PRODUCING PROVINCES (PRIMARILY ALBERTA, SASKATCHEWAN AND BC), FORESHADOW A POSSIBLE PROLONGED FEDERAL- PROVINCIAL STRUGGLE OVER TAX JURISDICTION. IN CONSEQUENCE, FUTURE OF CANADIAN RESOURCES INDUSTRY IS SOMEWHAT CLOUDY. GENERAL INDUSTRY RESPONSE HAS BEEN TO DEFER DEVELOPMENT AND INVESTMENT DECISIONS WHERE POSSIBLE, AND IN SOME INSTANCES TO CUT EXPLORATION ACTIVITIES, PENDING INITIALLY THE OUTCOME OF JULY 8 ELECTION. THIS IS A SERIOUS PROBLEM WHICH WILL HAVE TO BE FACED AND RESOLVED BY GOVERNMENT (FEDERAL AND PROVINCIAL) AND INDUSTRY IN MONTHS AHEAD REGARDLESS OF WHICH PARTY ASSUMES FEDERAL POWER.
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